

## Conferencia Interamericana de Seguridad Social



**Centro Interamericano de  
Estudios de Seguridad Social**

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BOOK REVIEW. PUBLIC POLICY FOR AN INCLUSIVE  
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# BOOK REVIEW. PUBLIC POLICY FOR AN INCLUSIVE GROWTH, EDITED BY PABLO COTLER

Alberto Huidobro Ortega\*  
Banco de México  
ahuidobr@banxico.org.mx

## Introduction

The book “Public Policy for an Inclusive Growth” (The book) is an opportune and fortunate document. It is opportune because it is presented at a time in which public policy topics are subject to a wide debate in Mexico, and the discussion is fed with diverse points of view, theoretical and political, from which it is the purpose to analyze, design, redesign, implement, and evaluate the government activity. It is opportune also due to the fact that it is presented in May of 2007, just days before the publication of the *Plan Nacional de Desarrollo 2007-2012*; which outlines the public policies’ orientation of President Felipe Calderon’s Administration, but allows room for the elaboration of the specific policies in charge of different specialized governmental bodies. Perhaps in the latter the proposals contained in The book could be included, if they succeed in influencing policy makers’ circles.

The book is fortunate because its design and presentation are adequate to a non-necessarily specialized audience, but one that has general knowledge of the relevant topics of the current public policy agenda. Moreover, it is fortunate because it gathers analysis and proposals from sixteen outstanding academics and specialists who have accumulated a deep knowledge of the subjects studied, as well as of the related policies and government programs in Mexico. Thus, the friendly and comprehensible style of the document does not undermine its foundation in thoughtful and rigorous analyzes elaborated by the authors.

On the other hand, The book covers a vast range of subjects of interest; starting with the analysis of the macroeconomic perspective—growth and macroeconomic policies—as a reference framework to explain the public policies in the country. Then it moves to specific subjects such as education, health care, the fight against inequality, regional development, credit market, federalism, among others. The reader will find, in all of them, perspectives worth of meditation, which deserve subsequent exploration to understand our reality, as well as to imagine better schemes and formulas for public policies in Mexico.

Given the vastness of the topics and the authors’ proficiency, it is a challenge to write a review of this book; for this reason I present some concrete opinions on a couple of subjects (rural financing and education) and a general comment at the end.

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\* Deputy Manager of Development Financial Institutions Analysis, Banco de Mexico. The opinions in this Review are strictly personal, and do not necessarily reflect the views of Banco de Mexico, its Board or its Staff.

The paper of Felix Velez, Alvaro Melendez and Helena Garcia proposes alternative ideas about rural financing on which I consider worth commenting:<sup>1</sup>

1. There is lack of financing to the rural sector;
2. Low-income households demand credit that is not served by formal institutions;
3. Only 7 per cent of the rural households receive loans from institutions or external (not household) sources, and,
4. The lowest proportion of the population that receives a formal credit is located in rural areas; it is in localities with less than 2,500 inhabitants that most people are in extreme poverty conditions, and they only have access to informal credit because of the lack of collateral.

Even when these claims describe realities in Mexico, the interpretation of these facts, in the sense of having a problem of lack of attention to an excess of credit demand in these areas, could ignore alternative views. For example, according to De la Torre et al. (2006) there is an important difference between ‘not receiving credit’ and a ‘problem of access to credit’. In their conceptual framework, De la Torre et. al argue that the problem of access is present when a project that would be financed with own capital, if it existed, does not receive external funding.<sup>2</sup> Moreover, they state that not having access to credit could reflect a poverty problem and not necessarily a problem of access to credit.<sup>3</sup> Besides this, it is worth asking how Velez, Melendez, and Garcia estimated the quantity demanded of credit and the credit supply, if they did, or how they calculated the excess demand of credit in the low-income market.

It is important to mention the contribution to this topic made by Pablo Cotler in this volume. Cotler sustains that, among the multiple factors that explain the unequal access to credit, the legal requirements to establish a financial relation stand out, because they represent important barriers to entry for the population employed in informal activities in the country; which he estimates as 40 per cent of the EAP.<sup>4</sup> Other factors are the lack of available information to measure the families’ income flow and the difficulty to know the credit history of these potential debtors. Both elements imply that interest rates are high and that a limited supply of financial products for these sectors is observed.

Hence, Cotler recommends:

- a) Accurate actions to make the industry of information more effective,<sup>5</sup>
- b) Increase the deregulation of the financial system and,
- c) Reforms to the development banks and the public programs system in order to “increase competition”.

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<sup>1</sup> See pages 161 and 162.

<sup>2</sup> Which implies that the project is financially viable; otherwise the person that is financing it would not risk its own funds. This idea can also be found in Huidobro (2004).

<sup>3</sup> Even more interesting, they point out that the imprudent access to credit could be a problem, since it has been seen as the cause of several financial crises worldwide.

<sup>4</sup> See p. 223. He also recognizes, besides the presence of asymmetrical information, the difficulty to demonstrate the property of assets eligible to be used as guarantees; this is often observed in rural areas as well as the difficulty of guaranteeing the creditors’ rights, at low cost, in case of bankruptcy (pp. 238-239).

<sup>5</sup> See pp. 230-233.

In this context it is worth highlighting and coinciding with the first point mentioned by Cotler with regard to credit information, especially when aware of recent proposals to erase the small debtors' records (even though the definition of "small" is not always clear) from the *Sociedades de Información Crediticia* (Credit Reporting Firms); In my opinion, its elimination would be an unwise destruction of relevant information. If records contain positive and negative behaviors, although only those negative are to be shared, both are important factors in the evaluation of the credit-risk. Furthermore, the small debtors are indeed those who suffer more the exclusion in the market because of the lack of credit-history.<sup>6</sup>

Another significant remark that Cotler<sup>7</sup> points out is that the lack of savings or of a continuous supply of loans may cause a productive insertion in sectors characterized by low costs of entry and operation, which generate low aggregate value and revenues; this could reinforce the poverty conditions even when it is recognized that indebtedness does not imply businesses success.<sup>8</sup> Moreover, he criticizes the government purpose of fighting poverty by means of credit granting, an strategy that might damage the development of a strong and stable industry in the savings and popular sector.

Notice that Cotler's critique, with which I agree, also applies to the recommendation made by Graciela Teruel and Luis Rubalcava in their document, when they point out the importance of generating mechanisms of access to productive credit for the whole population;<sup>9</sup> this last sentences seems to be in line either with the political speech frequently heard or with a somewhat utopian approach, especially in the presence of incipient patrimonies and reduced abilities and productive skills.

On the other hand, Velez, Melendez and Garcia criticize that institutions such as *Financiera Rural* or FIRA<sup>10</sup> have been "inefficient" and "non-equitable" as they tend to lend at subsidized rates to producers able to pay market interest rate, an idea apparently supported by previous studies.<sup>11</sup> They also argue that the development banks have inhibited the development of new intermediaries without displacing the informal lenders;<sup>12</sup> moreover, not even the interest rates have been reduced in the informal sector.<sup>13</sup>

They also point out that there is an excessive number of development institutions related to rural areas, which causes duplicities and inefficient competition in a relatively small market; this inefficiency raises as a consequence of a competitive offering of subsidies instead of services. They argue that it might be better to close these institutions as they only offer subsidized interest rates to producers able to pay market interest rates. They also suggest promoting cooperatives of savings and credit such as the *cajas de ahorro*, currently promoted by the *Banco del Ahorro Nacional y Servicios Financieros* (BANSEFI) to assist the financial needs of the rural sector.

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<sup>6</sup> In Huidobro (2000) development banks are assigned an important task of collection, processing, and dissemination of useful information to carry out credit operations.

<sup>7</sup> See pp. 207-208.

<sup>8</sup> Footnote 25, p. 227.

<sup>9</sup> See p. 357.

<sup>10</sup> Trust Funds in Relation with the Agriculture (*Fideicomisos Instituidos en Relación con la Agricultura*, FIRA), whose trustee is the Bank of Mexico.

<sup>11</sup> Such as Werner (1994), Huidobro (2000), Cotler (2000), Cotler (2003), and Huidobro (2004).

<sup>12</sup> A similar result is deduced from Armendariz (1999).

<sup>13</sup> As it has been already said, Cotler offers an explanation for this situation.

In this respect, I share the general reasoning of these authors, but I consider the solution proposed by them in the sense of closing the institutions mentioned above too drastic; a development bank reform in Mexico, which would consist of merging some institutions, among other actions,<sup>14</sup> might be a viable way to deal with the issue. On this subject, I agree with the specific idea that a more efficient scheme to assist the financial needs of the rural sector would be obtained if FIRA was merged to *Financiera Rural* and BANSEFI. Despite of this, a reform program of the Mexican development bank should not be based on the merging of institutions, only; but should consider a wide catalog of actions.<sup>15</sup>

It is also worth noticing that Velez, Melendez and Garcia are not aware of the apparent conflict of interest between BANSEFI and the popular institutions it should promote. The presence of the former could inhibit the proliferation of the latter. On the other hand, success of the popular institutions could question the future of BANSEFI; this to some extent, explains why the formalization process of the savings and popular credit sector has been slower than expected, as Cotler states; he also indicates that from a universe of 600 institutions, only 14 have been authorized by the *Comisión Nacional Bancaria y de Valores* (CNBV), and other 370 are in process—the deadline has been extended, possibly until 2012.<sup>16</sup>

Velez, Melendez and Garcia suggest tackling the problem of credit demand for profitable projects through training on the design of viable investment projects, as has been stated by World Bank (2003), Cotler (2003), and Cardenas and Huidobro (2004). On this matter, in his contribution Cotler adds the necessity of reducing the high costs of operation of the *financieras populares*, as well as the competition faced by these firms coming from public programs of direct credits (and subsidies).

Focusing on Cotler's work, it is worth mentioning some points:

1. Apparently, he admires that nowadays the Mexican government banks show capitalization indexes above the legally established, as well as provisions that almost double the non-performing loans. This is, of course, better than being in the opposite situation, but we should be aware of the fact that these indexes could also reveal certain degree of inefficiency in the use of bank resources.
2. Although he correctly explains the reasons why the interest rates of first-tier credit programs offered by some government bodies are lower than those charged by the popular saving and credit institutions,<sup>17</sup> and explains that these is an unfair competition to private counterparts, which generates negative externalities in this market, he apparently fails to recognize that those in fact do not constitute credit programs but funds provided under the logic of attempting to be recovered, without the definitive purpose of having them paid back, like in the case of the credit operations between financial institutions. It is worth noting that this characteristic of disguised subsidy has even more negative effects that the ones described by Cotler.

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<sup>14</sup> See Huidobro (2000), Huidobro (2004) and IMF-WB (2006).

<sup>15</sup> See Huidobro (2004).

<sup>16</sup> In fact, according to the Transitory Articles of the reforms to the Savings and Popular Credit Law, published on August 31, 2007, under certain circumstances these agencies could obtain authorization to formalize in a period that could be extended until December 31, 2012. See DOF (2007).

<sup>17</sup> Footnote 32, p. 234.

3. Among others, he proposes the following actions for the public intervention in financial services:<sup>18</sup> a) Target the objective population and justify the existence of public programs, b) Minimize possible overlaps among different programs and public institutions, c) Once this is done, integrate the programs under a single authority to guarantee its long term strategic planning.

It is worth noting that all these actions are compatible with what has been proposed by Huidobro (2004), as well as under the so called Performance Evaluation System (SED) proposed by the *Secretaría de Hacienda* (Treasury) on March, 2007. In fact, the SED proposes, based on a set of methodological elements, to evaluate the performance of government programs, its fulfillment of aims and objectives, and the use of strategic and management indicators to know the social impact of government programs and projects.

In this sense, the SED points out that the use of strategic indicators, "... will stimulate the budget's allocation in function of concrete results that can be objectively evaluated, ... and accountability and transparency will be promoted,..."

According to the proposal, the SED will be obligatory for all agencies that take part on the Federal Budget (PEF), and will be observed starting in the fiscal year 2009. As a first step the evaluation will be applied to the 124 main programs carried out by government agencies, which represent 27 per cent of the budget.

In regards to education, The book continuously makes reference to its importance, which is not unusual when accounting by its importance and the urgent necessity of solving the problems faced by the educational sector in Mexico.

For instance, Rodolfo de la Torre states that the programs of public expenditure that are more progressive are those of basic education services and health care for the excluded population; while the more regressive are those of tertiary education and social security systems.<sup>19</sup> He also finds that the higher inequalities in income distribution among groups are explained by differences in education and occupations.<sup>20</sup> Similarly, Carlos Muñoz and Marisol Silva sustain that the exclusion from the school system affects more the population in poverty,<sup>21</sup> which in my opinion anticipates a vicious circle of poverty and illiteracy among this population.

Graciela Teruel and Luis Rubalcava indicate that the capacity of the population to generate more income on their own continues to be the most important challenge to fight poverty in Mexico; hence, it is necessary to implement public policies that increase the productive capacity, that is, that overcome capacity deficits in the population.<sup>22</sup> For this reason, they propose to increase the investment in human capital.<sup>23</sup>

Eduardo Rodríguez-Oreggia emphasizes on the creation of human capital as a prerequisite to increase productivity and regional growth in order to fight the regional inequalities in the country.

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<sup>18</sup> See p. 236.

<sup>19</sup> See p. 71. It is worth mentioning that the work of Carlos Cruz and Gabriela Andrea Luna on health care, and the work of Carlos Muñoz and Marisol Silva on basic education in Mexico, propose concrete actions to advance in the solution of the problems in each subject (see pp. 269-272, and 309-311, respectively).

<sup>20</sup> See p. 73.

<sup>21</sup> See p. 282.

<sup>22</sup> See p. 346.

<sup>23</sup> See p. 355.

The increase in human capital should be reflected in improved labor skills, while public investment should reduce transaction costs, strengthen communication among local markets and increase ties with foreign trade.

Finally, Liliana Meza recommends increasing the average schooling achievement in the country but also its quality as one of the actions to improve the labor market, in order to elevate the productivity of the labor force.

Unfortunately The book does not include a sound and comprehensive chapter that revise in depth and under different perspectives the imperative need of designing a new educational policy, proposing concrete mechanisms to solve this sector's problematic, its internal resistances, its conflicts of interest; and propose actions to provide the correct incentives to operate, in my opinion, the essential structural reform that Mexico requires: an integral educational reform that provides enough human capital to put Mexico in a position internationally compatible with its importance and economic potential. A complementary document should discuss a strategy of technological modernization in all the country's fields and the best practices to achieve it.

In general terms, as any work of scientific research, The book could be improved and complemented with a second volume in which I suggest to include an updated and detailed study of the role of the government, and public policies in the current context, that is, in a XXI century characterized by the global opening, the presence of diverse and new actors, national and international, who influence the design of public policies and offer deeper and specific arguments and reasoning concentrated in the functions that correspond to a modern State: the provision of education services, health care, public surveillance, property rights protection, strict application of the law, etc.<sup>24</sup>

Besides, a second volume of Public Policies for an Inclusive Growth should approach the subject of fiscal policy compatible with the objectives of a new public policy agenda and its funding, from the medium and long term perspective. In that sense, it is not enough to recommend that public expenditure should be increased in a particular sector or policy; the arguments behind that could be true and valid, but incomplete, if the funds sustainability is not analyzed.

What would it be the general evaluation of The book? Excellent in my opinion. As can be seen in this brief review, its content informs and approaches current subjects of interest. This is done in a way that makes the reader interested in learning more about each subject; because with its comprehensible style invite to bring alternative ideas into the analysis, to participate in a debate on every subject that it covers, and to extend the subject menu, in order to offer a wider catalog of actions to work on, in order to procure a better future to the coming generations of Mexicans. In other words, I think The book succeeds in getting the readers involved in the discussion, design and implementation of public policies; especially in a country needed of quick and effective actions in a number of areas.

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<sup>24</sup> Although the work of Teruel and Rubalcava goes in this direction, a deeper and more comprehensive study is required.



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